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MEMORANDUM

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TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

EA for EGJ

Arizona Corporation Commission

DOCKETED

FEB 23 2005

DATE: February 23, 2005

DOCKETED BY

RL

RE: IN THE MATTER OF THE APPLICATION OF QWEST COMMUNICATIONS CORPORATION D/B/A QWEST LONG DISTANCE FOR EXTENSION OF ITS EXISTING CERTIFICATE OF CONVENIENCE AND NECESSITY TO INCLUDE AUTHORITY TO PROVIDE RESOLD AND FACILITIES-BASED LOCAL EXCHANGE AND RESOLD LONG DISTANCE SERVICES IN ADDITION TO ITS CURRENT AUTHORITY TO PROVIDE FACILITIES-BASED LONG DISTANCE SERVICES, AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES WITHIN THE STATE OF ARIZONA (DOCKET NO. T-02811B-04-0313)

Attached is the Staff Report for the above referenced Application. The Applicant is applying for approval to provide the following services in addition to the Facilities-Based Long Distance Service which it is already authorized to provide:

- Resold Local Exchange Services
- Facilities-Based Local Exchange Services
- Resold Long Distance Services

Staff is recommending approval of Qwest Communications Corporation d/b/a Qwest Long Distance's Application to amend its existing Certificate of Convenience and Necessity to include authority to provide statewide Resold Long Distance, in addition to the Facilities-Based Long Distance services it is already authorized to provide, and resold and facilities-based local exchange service outside of Qwest Corporation's current service area in accordance with the recommendations specified in this report.

EGJ/JFB/red

Originators: John F. Bostwick
Armando Fimbres

Attachment: Original and Thirteen Copies

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STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

QWEST COMMUNICATIONS CORPORATION
D/B/A QWEST LONG DISTANCE
DOCKET NO. T-02811B-04-0313

IN THE MATTER OF THE APPLICATION OF QWEST COMMUNICATIONS CORPORATION D/B/A QWEST LONG DISTANCE FOR EXTENSION OF ITS EXISTING CERTIFICATE OF CONVENIENCE AND NECESSITY TO INCLUDE AUTHORITY TO PROVIDE RESOLD AND FACILITIES-BASED LOCAL EXCHANGE AND RESOLD LONG DISTANCE SERVICES IN ADDITION TO ITS CURRENT AUTHORITY TO PROVIDE FACILITIES-BASED LONG DISTANCE SERVICES, AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES WITHIN THE STATE OF ARIZONA

FEBRUARY 23, 2005

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EXHIBITS:

TELECOMMUNICATIONS SERVICES BY STATE.....EXHIBIT A

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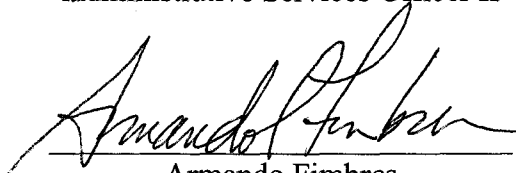
LOCAL EXCHANGE CALLING PLANS AND CHARGES.....EXHIBIT C

STAFF ACKNOWLEDGMENT

The Staff Report for Qwest Communications Corporation, Docket No. T-02811B-04-0313, was the responsibility of Staff members listed below. John Bostwick and Armando Fimbres were responsible for the review and analysis of the Application for a Certificate of Convenience and Necessity to provide resold long distance, resold local exchange, facilities-based long distance, and facilities-based local exchange telecommunications services and petition for a determination that its proposed services should be classified as competitive.



John F. Bostwick
Administrative Services Officer II



Armando Fimbres
Public Utility Analysis

1. INTRODUCTION

On April 23, 2004, Qwest Communications Corporation ("QCC" or "Applicant" or "Company") filed an Application to have its Certificate of Convenience and Necessity ("CC&N") modified to include resold long distance service, resold local exchange service, facilities-based long distance service, and facilities-based local exchange service.

On December 9, 2003, in Decision No. 66612, QCC d/b/a Qwest Long Distance ("QCC") was granted authority to provide facilities-based long distance telecommunications services throughout the State of Arizona. In the same decision, QCC's authority to provide resold long distance telecommunications services was revoked by the Commission.

On September 20, 2004, QCC filed a letter to amend its Application. In the September 20th Letter, QCC indicated its plans to provide telecommunications services in Arizona. QCC stated that it "... presently plans, and has therefore provided tariffs for, only one local exchange service. That product provides access from the local exchange to frame relay and asynchronous transfer mode ("ATM") services offered by several carriers." Only a tariff for Exchange Access Facilities was filed in the original Application.¹

On December 17, 2004, QCC filed a "Supplement to Application and Petition". QCC's filing supplements Section A-9 of its Application and Petition by adding a new proposed Local Exchange Services QCC Arizona Tariff No. 3. In addition providing a copy of the tariff as Attachment B, the filing revises QCC's responses concerning proposed rates and charges, for each service, tariff maximum rates and prices to be charged, terms and conditions applicable to the provision of service, and proposed a \$25.00 fee that will be charged for returned checks referenced as a tariff item in the Application.

In the supplement filing, QCC withdrew the Exchange Service Tariff QCC Arizona Tariff No. 3 that was included in its original Application. Also, the statements made in the September 20th Letter were withdrawn.

The Applicant petitioned the Arizona Corporation Commission ("Commission") on December 17, 2004, for a determination that its proposed services should be classified as competitive. In its supplement filing, QCC provided Staff with a new proposed Local Exchange Services QCC Arizona Tariff No. 3.

The tariff pages provided on December 17, 2004, in the Local Exchange Services QCC Arizona Tariff No. 3 were incomplete. QCC filed a Notice of Errata on January 12, 2005. QCC submitted tariff pages to correct the information omitted in the supplement.

Staff's review of this Application addresses the overall fitness of the Applicant to receive a CC&N. Staff's analysis also considers whether the Applicant's services should be classified as competitive and if the Applicant's initial rates are just and reasonable.

¹ Exchange Service Tariff QCC Arizona Tariff No. 3 submitted with the Application did not reflect the services that were being requested by QCC. QCC Arizona Tariff No. 3 was withdrawn on September 20, 2004.

2. QCC'S APPLICATION FOR EXTENSION OF ITS CERTIFICATE OF CONVENIENCE & NECESSITY

This section of the Staff Report contains descriptions of the geographic market to be served by the Applicant, the requested services, and the Applicant's technical and financial capability to provide the requested services.

2.1 DESCRIPTION OF THE GEOGRAPHIC MARKET TO BE SERVED

QCC is seeking additional authority to provide resold and facilities-based local exchange and resold long distance telecommunications services throughout the State of Arizona. The Company is already certificated to provide facilities-based long distance services throughout the State of Arizona.

2.2 THE ORGANIZATION

QCC is incorporated under the laws of the State of Delaware and has been authorized to do business in Arizona since June 6, 1989. QCC is a wholly owned subsidiary of Qwest Services Corporation ("QSC"), which in turn is a wholly owned subsidiary of Qwest Communications International, Inc. ("QCII").

Qwest Corporation ("QC"), which is a wholly owned subsidiary of QCII, is an incumbent local exchange carrier and Bell Operating Company as defined by the Telecommunications Act of 1996, providing both local and intraLATA long distance services throughout much of Arizona. QC was authorized by the FCC to provide interLATA long-distance service in Arizona on December 15, 2003. With approval of QC's Section 271 application under the 1996 Act, interLATA services may be provided only through a wholly separate Qwest Corporation affiliate ("Section 272 Affiliate").

QCC received a CC&N to provide facilities-based interexchange intraLATA and interLATA long-distance service in Arizona on December 9, 2003. QCII also established Qwest LD Corp. d/b/a Qwest Long Distance ("QLDC") as a wholly owned subsidiary of QSC. On December 9, 2003, in Decision No. 66613, QLDC was granted authority to provide competitive resold interexchange interLATA and intraLATA long-distance services in Arizona. QLDC was formed to provide resold in-region long distance service to residential consumers which also have QC as their local provider.

2.3 THE APPLICANT

QCC intends to be both a reseller and a facilities-based provider of long distance and local exchange telecommunications services in Arizona. In its Application, QCC indicated that it does business under the d/b/a Qwest Long Distance for its interexchange business.

QCII indicated that it intends to utilize QCC to serve residential customers (which have another carrier as their local service provider) and business customers (which have QC or another carrier as their local service provider) as a facilities-based provider (in all of its in-region states), at least until the point at which the businesses of QLDC and QCC can be combined.

Both QCC and QLDC operate as Section 272 Affiliates of Qwest Corporation. None of the officers or directors of QCC have any direct ownership interest in QCC. QCII, the ultimate parent company of QCC, is a publicly traded entity on the New York Stock Exchange. Both Companies must comply with the other requirements of Section 272 as well.

On September 21, 2004, QC submitted to the Commission for approval an interconnection agreement entered into with QCC. The agreement was approved by operation of law on December 20, 2004. QCC has not yet filed for approval with the Commission any interconnection agreements with other independent incumbent local exchange carriers in the state.

QCC has been named in formal and informal proceedings before state and federal commissions with responsibility for telecommunications regulation. QCC does not track each formal or informal complaint filed against it in any centralized system. QCC does track, however, actions or investigations initiated by state or federal utility commissions, attorneys general, or consumer advocate offices, and similar agencies or entities, which are described in Section 4.

2.4 TECHNICAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

QCC indicated that it has been approved as a Competitive Local Exchange Carrier ("CLEC") in Washington, Oregon, Utah, Montana, Idaho, Iowa, Minnesota, Colorado and Wyoming. Also, QCC states that it has been approved to provide competitive local exchange and/or resold long distance service in 45 states, excluding Arizona (See attached Exhibit A).

Currently, QCC is a certified facilities-based provider of interexchange services and other services in every state except Alaska. As a result of QCC's certification status and the telecommunications services it provides, Staff believes QCC possesses the technical capabilities to provide the services it is requesting the authority to provide.

2.5 FINANCIAL CAPABILITY TO PROVIDE THE REQUESTED SERVICES

QCC indicated in its Application that it will rely on the financial resources of its parent company QSC. QCC provided audited financial statements, with notes, for the year ended December 31, 2003 for its ultimate parent company, QCII. These financial statements list assets in excess of \$26.2 billion; negative equity of \$1.0 billion; and a net loss of \$1.5 billion. Exhibit B compares QCII's financial ratios to the average financial ratios of the telecom industry.

As part of its supplement to the Application, QCC filed a revised tariff and indicated in

Section 2 on page 13 of its QCC Arizona Tariff No. 3 that it collects advances and deposits from its customers. Staff believes that advances, deposits, and/or prepayments received from the Applicant's customers should be protected by the procurement of a performance bond. Since the Applicant is requesting a CC&N for more than one kind of service, the amount of a performance bond for multiple services is an aggregate of the minimum bond amount for each type of telecommunications service requested by the Applicant. The amount of bond coverage needed for each service is as follows: resold long distance \$10,000 for advances, deposits and/or prepayments collected; resold local exchange \$25,000; facilities-based long distance \$100,000; and facilities-based local exchange \$100,000. The bond coverage needs to increase in increments equal to 50 percent of the total minimum bond amount when the total amount of the advances, deposits, and prepayments is within 10 percent of the total minimum bond amount. Further, measures (as discussed below) should be taken to ensure that the Applicant will not discontinue service to its customers without first complying with Arizona Administrative Code ("A.A.C.") R14-2-1107.

QCC stated in its Application that it has already posted a \$100,000 performance bond as a facilities-based long distance provider as required for its CC&N in Decision No. 66612. To that end, Staff recommends that the Applicant procure another performance bond equal to \$135,000. The minimum bond amount of \$135,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers, in the manner discussed above. The bond amount, therefore, should be increased in increments of \$67,500. This increase should occur when the total amount of the advances, deposits, and prepayments is within \$13,500 of the bond amount.

If the Applicant desires to discontinue service, it must file an application with the Commission pursuant to A.A.C. R14-2-1107. Additionally, the Applicant must notify each of its customers and the Commission 60 days prior to filing an application to discontinue service. Failure to meet this requirement should result in forfeiture of the Applicant's performance bond. Staff further recommends that proof of the above mentioned performance bond be docketed within 365 days of the effective date of an Order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission.

If at some time in the future, the Applicant does not collect from its customers advances, deposits, and/or prepayments, Staff recommends that the Applicant be allowed to file a request for cancellation of its established performance bond regarding its resold long distance services. Such request must reference the decision in this docket and must explain the Applicant's plans for canceling those portions of the bond.

If QCC experiences financial difficulty, there should be minimal impact to its customers because there are many other companies that provide resold telecommunications services or the customers may choose a facilities-based provider. If the customer wants service from a different provider immediately, that customer is able to dial 1+101XXXX access code. In the longer term, the customer may permanently switch to another company.

2.6 QCC'S COMPLIANCE WITH DECISION NO. 66612

Staff was instructed through a Procedural Order dated February 1, 2005, to address QCC's compliance requirements of Decision No. 66612, including but not limited to Finding of Facts No. 59, in its Staff Report in this docket. The Procedural Order also required Staff to address the scope and the status of the joint Federal/State independent audit required of QCC's affiliate QC regarding its competitive affiliates under §272 of the Telecommunications Act of 1996. In addition, the Procedural Order directed Staff to address the issue of whether the reaffirmation of the limited waiver of the Commission's Affiliated Interests Rules granted in Decision No. 64654 should be revisited, in light of the fact that QCC is requesting authority to provide services in competition with services provided by its affiliate QC.

Section 2.6 of this Staff Report addresses the compliance requirements of Decision No. 66612 regarding the Finding of Facts No. 59. The scope and the status of the joint Federal/State independent audit required of QCC's affiliate QC is addressed in Section 2.7 of this report. The issue of whether the reaffirmation of the limited waiver of the Commission's Affiliated Interests Rules granted in Decision No. 64654 is addressed in this report under Section 2.8.

In Decision No. 66612, the Commission ordered Staff to monitor QCC's filings of copies of any and all contracts and/or agreements, written or verbal, between QCC and its affiliates to ensure that QCC and its affiliates are not engaging in anticompetitive behavior (refer to Finding of Facts No. 59). Also, QCC is required to submit copies to Staff of its contracts and agreements with its affiliates within thirty days of execution.

QC is required under 47 U.S.C. Section 272 to list each contract and agreement it has with its affiliate, QCC, on its website. A competing carrier can access QC's website and identify the contracts and/or agreements QC has with QCC and review contracts and/or agreements in detail. If the carrier believes that the reviewed contract and/or agreement suggests or encourages anticompetitive behavior, the carrier can file a complaint against QC and/or QCC with the Commission.

Under 47 U.S.C. Section 272, QC is not required to list on its website contracts/or agreements between QCC and its other affiliates. Contracts and/or agreements between QCC and its other affiliates are sent to Staff.

Staff has reviewed QC's website and determined that contracts and/or agreements with its affiliate, QCC, are listed on QC's website. In addition, Staff has reviewed the execution date and the date submitted of a sample of the contracts and/or agreements to ensure QCC's filings are submitted within thirty days. Staff has informed QCC, in writing, that four of the sample contracts and/or agreements were filed late. At this time, Staff is not aware of any complaint filed by another carrier against QCC and/or QC alleging anticompetitive conduct.

2.7 FEDERAL/STATE INDEPENDENT AUDIT

Section 272(a) of the Communications Act of 1934, as amended ("the Federal Act"), requires that a Bell Operating Company ("BOC") set up one or more separate affiliates to provide, inter alia, in-region interLATA services. Section 272(d) requires a BOC to obtain and pay for a joint Federal/State audit every two years.

The FCC adopted rules to implement the Section 272(d) biennial audit requirement. See Accounting Safeguards Order; see also 47 C.F.R. Section 53.209 et seq. The purpose of the Section 272(d) biennial audit is to determine whether the BOC and its Section 272 affiliates have operated in accordance with the accounting and non-accounting safeguards required by section 272 of the Federal Act and the FCC's rules. The FCC's rules also provide for the establishment of a Federal/State joint audit team that is authorized to oversee the conduct of the audit from the planning stage to its completion and to direct the independent auditor to take any actions necessary to ensure compliance with the audit requirements. Although the section 272(d) biennial audit is to be conducted by an independent auditor, the Federal/State joint audit team is also responsible for ensuring that the audit meets the objectives stated in the FCC's rules and orders.

The first biennial audit examined Qwest Communications International, Inc.'s ("QCII") compliance with the requirements of Section 272 during the period January 2, 2003 to January 1, 2004. The Joint Oversight Team was composed of staff members from 12 state regulatory agencies within Qwest's region, including Arizona, and the FCC. On June 8, 2004, Ernest & Young LLP filed its "Report of Independent Accountants on Applying Agreed-Upon Procedures".

Staff docketed the Ernest & Young Report on June 18, 2004, and gave interested parties an opportunity to comment on the Report. To the best of Staff's knowledge and belief, no comments have been filed on the Report.

2.8 WAIVER TO AFFILIATED INTERESTS RULES

In Decision No. 64654, QCC, QC, their affiliates, and their parent QCII were granted a limited waiver of A.A.C. R14-2-803 subject to the following conditions:

- a. QCC, QC, their affiliates, and their parent QCII are required to file a notice of intent to organize or reorganize a public utility holding company for those organizations or reorganizations that are likely to: 1) result in increased capital cost to Qwest Corporation; 2) result in additional costs allocated to the Arizona jurisdiction or 3) result in a reduction of Qwest Corporation's net operating income.
- b. QC shall file annually, at the time it provides the information required by A.A.C. R14-2-805, an affidavit from its Chief Executive Officer that lists the transactions for which QCC, QC, and their parent QCII, or any of their affiliates, has not filed

a notice of intent pursuant to the limited waiver granted herein, and which certifies that such transactions will not result in either increased capital costs to QC, additional costs being allocated to the Arizona jurisdiction, or reduction of QC's net operating income.

Since Staff is recommending that QCC provide competitive resold and facilities-based local exchange service throughout the State of Arizona except areas inside QC's service territory, Staff believes that the limited waiver of the Commission's Affiliated interests Rules granted in Decision No. 64654 (March 25, 2002) does not need to be revisited.

3. FACILITIES-BASED AND/OR RESOLD LOCAL EXCHANGE SERVICES AND RESOLD LONG DISTANCE SERVICE

This section of the Staff Report contains a description of the actual services to be provided by the Applicant. It also contains a discussion of the Company's tariffs and price lists. This section also contains Staff's analysis of any issues that were considered by Staff in arriving at its recommendation in this case. In addition, this section indicates Staff's evaluation of the Applicant's proposed rates and charges and Staff's recommendation thereon.

3.1 ACTUAL SERVICES TO BE PROVIDED AND PROPOSED SERVICE AREA

QCC indicated in response to Staff data requests, that with specific reference to telemarketing efforts, generally, QCC will target medium and large business and government customers with needs for both local and interexchange voice and data services. QCC indicated in its December 2004 supplement to its Application that its proposed local exchange service would consist of offerings to business customers at this time. The business services it intends to immediately offer include: but are not limited to the following: Basic Local Voice; Direct-Inward-Dialing Services; Custom Calling Services; Hunting Services; Directory Listing Services; Local Operator Services; Local Directory Assistance Service; Screening and Restriction Services; Caller Identification Blocking Options; intraLATA, intraexchange private line services; Customer Premises Wire and Maintenance Plans; and ISDN PRI services. The tariff for these services was included in the Supplement to Application and Petition filing dated December 17, 2004.

QCC indicated in response to Staff data requests that grant of its request to act as a CLEC in QC's service territory would allow it to provide a single contract and an integrated bill to business customers for local and long distance services. QCC further stated that many requests for proposals require that a responding entity be able to provide services through a single contract and a unified bill and customer relationship, and not deliver the requested services through different entities, billing mechanisms, or affiliates. According to QCC, many customers, whether or not a formal RFP is involved, desire this "one stop shopping" because it provides a simple, straightforward means to address various issues or concerns that may arise about its service, i.e., a single contact for purposes of repair and inquiries as well as a unified bill.

Staff recommends that QCC's request to provide statewide interLATA and intraLATA long distance service on a resold basis be granted by the Commission, subject to the conditions below. Staff also recommends that QCC's request to provide competitive resold and facilities-based local service be approved but that it is confined initially to areas outside of QC's service territory, subject to the conditions below.²

QCC's request to provide local exchange services as a CLEC within the service territory of its affiliate and incumbent QC's local service area raises difficult issues that have not been satisfactorily addressed by the Company's application. These unresolved concerns encompass, *inter alia*,

1. The ability of QCC to leverage QC's ILEC position and engage in anti-competitive conduct including but not limited to cross-subsidization and, price-squeezing;
2. The potential for significant confusion on the part of customers given the similarity in names;
3. Use of QCC (the CLEC) to evade QC's (the ILEC) obligations within QC's service territory.
4. The potential for discrimination by QC
5. Whether it is in the public interest for an RBOC to have an affiliated CLEC operating within its territory, when the local market is not sufficiently competitive.

The initial exclusion of areas served by QC will help to ensure that QCC does not have an unfair advantage over other CLECs by leveraging QC's ILEC position. Even though as discussed below, Section 272 should operate to address many anticompetitive concerns, it does not address all of Staff's concerns in this regard. In addition to this, there is far too great a potential given the similarity of names to create confusion in the minds of the public. The opportunity for evasion by QC of its regulatory obligations is also a very real concern at this time as discussed below. Finally, the local market in QC's service territory is not sufficiently competitive so that if abuses did occur, they would be more likely at this point in time to have a devastating effect on the development of competition in Arizona. Allowing QCC to initially provide CLEC services only to customers who are not already served by its incumbent affiliate QC, will allow QCC to compete against other CLECs and ILECs as requested in its Application, outside of QC's ILEC territories. QC will continue to serve areas in which it is the designated ILEC and will retain its regulatory obligation to provide telephone service as a Carrier of Last Resort ("COLR").

Staff recognizes that some states within Qwest's in-region footprint, as well as some states nationwide have approved applications by an RBOC CLEC affiliate to provide service in the BOC's in-region service territories.³ Indiana has approved such an application with

² This should in no way be construed as a finding under Section 251 (f) of the Telecommunications Act of 1996.

³ See, In the Matter of the Application of Qwest Communications Corporation to Amend its Certificate of Authority to Provide Facilities-Based and Resold Local Service, Minnesota Public Utilities Commission Docket No. P-5096/M-03-1401, Order Granting Application Subject to Conditions and Setting Operational Requirements, (December 11, 2003), In Re: Qwest Communications Corporation, Iowa Utilities Board Docket Nos. TCU-03-13,

extensive conditions, including imposition of unbundling and resale obligations and with a further condition that the affiliate could not offer voice services.⁴ Nebraska will only allow affiliate companies to compete in their ILEC territory under very limited conditions which include instances where there are multi-location business customers both in and out of the ILEC region. In order to have the restrictions removed, the ILEC must show that the market is sufficiently competitive.⁵ Other states have only approved such applications for the provision of advanced services.⁶ Some states apparently will not allow such BOC CLEC affiliates to provide voice service within the BOC ILEC territory.⁷ At least one other state has certificated the BOC CLEC affiliate to operate outside of its BOC ILEC's service territory.⁸

WRU-03-48-419, Order Approving Amendment to Approved Application (November 29, 2004), In the Matter of Qwest Communications Corporation Application for a Certificate of Authority to Provide Telecommunications Service and Classification as a Competitive Provider, Oregon Public Utility Commission CP 1041 et seq., Order, (June 14, 2002), In the Matter of the Application of qwest Communications Corporation for Approval to Operate as a Facilities-Based Carrier in the State of Utah, Docket No. 94-2204-01, Report and Order, (Issued August 21, 1995), In Re Application of BellSouth BSE, Inc. for a Certificate of Public Convenience and Necessity to Provide Local Exchange Telecommunications Service in the State of South Carolina, Order Approving Certificate to Provide Service, Docket No. 97-361-C, Order No. 97-1063 (December 23, 1997); Joint Application of BellSouth BSE, Inc., and BellSouth Long Distance, Inc. for Approval of Merger, Order Granting Motion and Joint Application, Public Service Commission of South Carolina Docket No. 2004-45-C, Order No. 2004-299 (June 18, 2004); In the Matter of the Petition for An Order Authorizing VIC-RMTS-DC, LLC d/b/a One Point Communications n/k/a Verizon Avenue to Provide Local Exchange and Interexchange Telecommunications Services Throughout New Jersey, Docket No. TE00060345, Order of Approval (February 20, 2002); Application of Southwestern Bell Communication Services, Inc., for Intrastate Authority to Resell Telecommunications Services and for Certification as a Telecommunications Utility-Reseller, Public Service Commission of Wisconsin Docket No. 7182-TI-101 (July 11, 2003); In the Matter of BellSouth BSE, Inc., Application for Certificate of Public Convenience and Necessity to Provide Local Exchange and Exchange Access Telecommunications Services in North Carolina, Order Granting a Certificate of Public Convenience and Necessity, Docket No. p-691 (July 22, 1998); See also Application for Approval to Merge BellSouth BSE, Inc. into BellSouth Long Distance, Inc., and for Authority to Operate Bellsouth Long Distance, Inc. as a Competing Local Provider Docket Nos. P-654, 'Sub 5, P-691, Sub 1., Order Approving Merger and Granting Certificate (September 24, 2004).

⁴ In the Matter of the Petition of Ameritech Advanced Data Services of Indiana, Inc. for a Certificate of Territorial Authority to Provide Facilities-Based and Resold Telecommunications Services Throughout the State of Indiana and Requesting the Commission to Decline to Exercise Jurisdiction Pursuant to I.C. 8-1-2.6, Indiana Utility Regulatory Commission Cause No. 41660, Approved March 19, 2001.

⁵ In the Matter of the Application of Qwest Communications Corporation seeking authority to operate as a competitive local exchange carrier of telecommunications services within the state of Nebraska, Application No. C3201, (December 14, 2004); including limitations ordered in the Investigation into the effects of incumbent local exchange carriers using affiliates to compete within their own territory, Application No. C-1839/PI-22 (December 15, 1998).

⁶ In the Matter of Application of SBC Advanced Solutions, Inc. for a Certificate of Convenience and Authority to Transact the Business of a Telecommunications Carrier for the Purpose of Providing Advanced Data Services and Other Telecommunications Services Within the State of Kansas and for Approval of its Initial Tariff, Docket No. 00-SBAT-247-COC (January 13, 2000); Public Utility Regulatory Act, TEX. UTIL. CODE ANN. Section 54.102.

⁷ In the Matter of Application of SBC Advanced Solutions, Inc. for a Certificate of Convenience and Authority to Transact the Business of a Telecommunications Carrier for the Purpose of Providing Advanced Data Services and Other Telecommunications Services Within the State of Kansas and for Approval of its Initial Tariff, Docket No. 00-SBAT-247-COC (January 13, 2000); Public Utility Regulatory Act, TEX. UTIL. CODE ANN. Section 54.102. In Texas, the Public Utility Regulatory Act section 54.102 allows a BOC's affiliate CLEC to provide advanced services in the BOC's serving area. However, such an affiliate may not provide flat rate local exchange services to residential and business customers in the BOC's serving area.

⁸ In re Application of BellSouth Telecommunications, Inc., for a Certificate for Convenience and Necessity to Provide Exchange and Exchange Access Service as a Competitive Local Exchange Carrier in Alabama, Docket No. 27663, Report and Order, (September 13, 2000).

Section 272 does alleviate some of Staff's concerns. Indeed the FCC has found that nothing in the Federal Act precludes a Section 272 BOC affiliate from providing local exchange and exchange access:

Based on our analysis of the record and the applicable statutory provisions, we conclude that section 272 does not prohibit a section 272 affiliate from providing local exchange service in addition to interLATA services, nor can such a prohibition be read into this section. Specifically, section 272(a) (1) states that— A Bell operating company (including any affiliate) which is a local exchange carrier that is subject to the requirement of section 251(c) may not provide any service described in [section 272(a) (2) unless it provides that service through one or more affiliates that ... are separate from any operating company entity that is subject to the requirements from section 251(c)...

We find that the statutory language is clear on its face – a BOC section 272 affiliate is not precluded under section 272 from providing local exchange service, provided that the affiliate does not qualify as an incumbent LEC subject to the requirements of section 251(c).⁹

However, Section 272 does not resolve all of Staff's concerns. Second, Staff is concerned given QCC's responses to Staff data requests, if and how QC intends to share its Customer Proprietary Network Information ("CPNI") with QCC and any competitive advantage that this may bestow upon QCC. QCC will have access to QC's CPNI and no other CLEC will have such access. In addition, the Section 272 requirements do not resolve Staff's concerns regarding confusion to the public given use of the "Qwest" brand name and QC's use of QCC to evade its regulatory responsibilities under the Act. In response to Staff's data requests, QCC indicated that it will use the informal brand name "Qwest" to market its CLEC services.

The FCC has itself many times stated that a BOC can not use an affiliate to evade its regulatory obligations under Sections 251, 252 and 271 of the Act.¹⁰ If QCC is allowed to operate as a CLEC in QC's LLEC service area in Arizona, we believe this would permit QC to avoid its regulatory obligations under Sections 251, 252 and 271 of the 1996 Act.

Staff is also mindful of the provisions of Section 47 U.S.C. 253(a) which provide in relevant part that: "No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service." However, Section 253(b) provides that "Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of

⁹ In the Matter of Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, CC Docket No. 96-149, First Report and Order at para. 312 (rel. December 24, 1996).

¹⁰ See, inter alia, In the Matter of the Application of SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. D/B/A Southwestern Bell Long Distance Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Texas, CC Docket No. 00-65, Memorandum Opinion and Order, para. 409 (June 30, 2000).

telecommunications services, and safeguard the rights of consumers.” Staff believes that its recommendations in this case are necessary to protect the development of competition in QC’s service territory and ensure that all providers are treated on a competitively neutral basis. There is not sufficient competition in QC’s in-region local exchange territory in Arizona to guard against any abuses that may occur. In Nebraska, an affiliate of QC cannot offer local exchange service in competition with QC, until stringent criteria have been met or there is a sufficiently competitive local exchange market.¹¹ In addition, QC has the ability itself under the Arizona Commission’s rules to have services classified as competitive under the Competitive Classification Rules, R14-2-1109 et. seq.

Thus, it is Staff’s recommendation that QCC should initially be approved to provide service in exchanges where incumbent local exchange carriers (“ILECs”), other than QC, are providing telephone services. QCC, with Commission approval, will be able to compete against other providers, other than QC, by offering local exchange services to potential customers throughout the State of Arizona, excluding areas served by QC. As a result, QCC would generally not have a competitive advantage in areas where Qwest’s ILEC market position is recognized by customers. Staff is concerned that such an immediate competitive advantage would be a detriment to local exchange competition.

The condition that QCC should initially be approved to provide service in exchanges where incumbent local exchange carriers (“ILECs”), other than QC, are providing telephone services is consistent with the CC&Ns granted to four other competitive carriers in Arizona that have ILEC affiliates. The four companies that received CC&Ns to provide competitive telecommunications services in areas where their ILEC affiliate is not certificated to provide telecommunications services are Rural Network Services, Inc., Valley Connections L.L.C., Electric Lightwave, Inc., and Verizon Select Services Inc. The CC&N decision(s) for each is as follows: Rural Network Services, Inc. (Decision No. 66841), Valley Connections L.L.C. (Decision No. 66846), Electric Lightwave, Inc. (Decision Nos. 59982 and 60293), and Verizon Select Services Inc. (Decision No. 63546). To the best of Staff’s knowledge, these are the only four certificated Arizona CLECs that have ILEC affiliates.

Finally, in its response to Staff data requests, QCC indicated that it does not intend to provide service in unserved areas at this time. While other CLECs have been certificated on a statewide basis, no CLEC to Staff’s knowledge has attempted to use its statewide CC&N to provide service in unserved areas. Should this occur, we believe that unique issues would arise including the applicability of the competitive classification rules and findings to areas of the state in which the CLEC is the only provider. In this circumstance, Staff may find that the competitive classification rules and findings under those rules in CLEC CC&N’s are not applicable in unserved areas and that classification as an ILEC is more appropriate. Staff intends to address this issue at the time a CLEC notifies Staff that it intends to provide service in an unserved area. As part of its certification, Staff recommends that the Commission include a condition that QCC notify the Commission prior to providing service to any unserved areas of the State.

¹¹ In the Matter of the Application of Qwest Communications Corporation seeking authority to operate as a competitive local exchange carrier of telecommunications services within the state of Nebraska, Application No. C-3201 (December 14, 2004).

3.2 PROPOSED RESOLD AND/OR FACILITIES-BASED LOCAL EXCHANGE TARIFF AND PRICE LISTS

Both an initial rate (the actual rate to be charged) and a maximum rate must be listed for each competitive service offered, provided that the rate for the service is not less than the Company's total service long-run incremental cost of providing the service pursuant to A.A.C. R14-2-1109.

Staff has reviewed the tariff and the proposed price list rates of QCC. Exhibit C (attached) shows selected local exchange calling plans and charges of QCC and other competitive carriers of the telecommunications services industry. Given the information available to Staff and its findings under Sub-section 3.3 below, Staff believes that QCC's rates are reasonable and should be approved.

QCC's tariff, however, does need to be modified to reflect the limitation Staff proposes on the service area for QCC's provision of resold and facilities-based local exchange service. In addition, QCC needs to modify its Arizona Tariff No. 3 Section 2.2.5 item E to ensure that local exchange telecommunications services will not be provided to business customers participating in the Competitive Response Program.

3.3 FAIR VALUE RATE BASE CONSIDERATION

Staff obtained information from QCC regarding its fair value rate base. As reported in the Applicant's Application, QCC's fair value rate base is \$5.8 million. However, the rate to be ultimately charged by QCC for the resold and facilities-based local exchange service(s) and resold long distance service outside of QC's service territory will be influenced by the market.

While Staff has considered the Applicant's fair value rate base, it has not afforded it substantial weight in this analysis since the rates proposed by this filing are for competitive services which are not required to be set according to traditional rate of return regulation. Staff has reviewed the rates to be charged by the Applicant and believes that they are just and reasonable as they are comparable to other competitive local carriers, local incumbent carriers and major long distance carriers currently operating in Arizona. See Sub-section 3.2 above.

3.4 DIRECTORY LISTINGS AND DIRECTORY ASSISTANCE

Callers should be able to determine the telephone numbers belonging to customers of alternative local exchange companies, such as the Applicant. Staff recommends that the Applicant file a plan that describes how it plans to have its customers' telephone numbers included in the incumbent's Directories and Directory Assistance databases before it begins providing local exchange service. This plan must be filed within 365 days of the effective date of the Order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission.

3.5 NUMBER PORTABILITY

Another issue associated with the Applicant's proposal to become a competitive local exchange company relates to how telephone numbers should be administered. Local exchange competition may not be vigorous if customers, especially business customers, must change their telephone numbers to take advantage of a competitive local exchange carrier's service offerings. Staff recommends that the Applicant pursue permanent number portability arrangements with other LECs that are consistent with federal laws, federal rules and state rules.

3.6 PROVISION OF BASIC TELEPHONE SERVICE AND UNIVERSAL SERVICE

The Commission has adopted rules to address the level of funding for universal telephone service during and after the transition to a competitive telecommunications services market. The rules contain the terms and conditions for contributions to and support received from telephone service subscribers in order to maintain the Arizona Universal Service Fund ("AUSF"). Under the rules, the Applicant will be required to contribute to the AUSF and it may be eligible for AUSF support. Therefore, Staff recommends that approval of the application for a CC&N be conditioned upon the Applicant's agreement to abide by and participate in the AUSF mechanism established by Decision No. 59623, dated April 24, 1996 (Docket No. RT-00000E-95-0498).

3.7 QUALITY OF SERVICE

Staff believes that the Applicant should be ordered to abide by the quality of service standards that were approved by the Commission for Qwest (f/k/a USWC) in Docket No. T-01051B-93-0183 (Decision No. 59421). Because the penalties that were developed in this docket were initiated only because Qwest's level of service was not satisfactory, Staff does not recommend that those penalties apply to the Applicant. In the competitive market that the Applicant wishes to enter, the Applicant generally will have no market power and will be forced to provide a satisfactory level of service or risk losing its customers. Therefore, Staff believes that it is unnecessary to subject the Applicant to those penalties at this time.

3.8 ACCESS TO ALTERNATIVE LOCAL EXCHANGE SERVICE PROVIDERS

Staff expects that there will be new entrant providers of local exchange service who will install the plant necessary to provide telephone service to, for example, a residential subdivision or an industrial park much like existing local exchange companies do today. There may be areas where the Applicant installs the only local exchange service facilities. In the interest of providing competitive alternatives to the Applicant's local exchange service customers, Staff recommends that the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve such areas. This way, an alternative local exchange service provider may serve a customer if the customer so desires. Access to other providers should be provided pursuant to the provisions of the 1996 Telecommunications Act, the rules promulgated there under and Commission rules on interconnection and unbundling.

3.9 911 SERVICE

The Applicant has indicated in its application that it will provide all customers with 911 and E911 service, where available, or will coordinate with ILECs and emergency service providers to provide the service. Staff believes that the Applicant should be required to work cooperatively with local governments, public safety agencies, telephone companies, the National Emergency Number Association and all other concerned parties to establish a systematic process in the development of a universal emergency telephone number system. Staff recommends that the Applicant be required to certify, through the 911 service provider in the area in which it intends to provide service, that all issues associated with the provision of 911 service have been resolved with the emergency service providers before it begins to provide local exchange service, within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission.

3.10 CUSTOM LOCAL AREA SIGNALING SERVICES

In its decisions related to QC's proposal to offer Caller ID and other CLASS features in the State, the Commission addressed a number of issues regarding the appropriateness of offering these services and under what circumstances it would approve the proposals to offer them. The Commission concluded that Caller ID could be offered provided that per call and line blocking, with the capability to toggle between blocking and unblocking the transmission of the telephone number, should be provided as options to which customers could subscribe with no charge. The Commission also approved a Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated, which indicates that the number has been blocked. The Commission further required that QC engage in education programs when introducing or providing the service(s).

Staff recommends that the Applicant be required to abide by all the Commission decisions and policies regarding Caller ID and other CLASS services. However, Staff does not believe that it is necessary for the Applicant to engage in the educational program that was ordered for QC as long as customers in the areas where the Applicant intends to serve have already been provided with educational material and are aware that they can have their numbers blocked on each call or at all times with line blocking.

3.11 EQUAL ACCESS FOR INTEREXCHANGE CARRIERS

The Applicant indicated that its switch will be "fully equal access capable" (i.e. would provide equal access to interexchange companies). The Commission requires local exchange companies to provide 2-Primary Interexchange Carriers ("2-PIC") equal access. 2-PIC equal access allows customers to choose different carriers for interLATA and intraLATA toll service and would allow customers to originate intraLATA calls using the preferred carrier on a 1+ basis. Staff recommends that the Applicant be required to provide 2-PIC equal access.

4. REVIEW OF COMPLAINT INFORMATION

This section of the Report addresses the complaint history of QCC.

4.1 COMPLAINT INFORMATION

QCC has settled formal complaint actions or investigations regarding alleged slamming or cramming activities with the following entities: the Federal Communications Commission ("FCC"), the state utility commissions of Oklahoma, South Dakota, Kentucky, Tennessee, Texas, and New Jersey; the attorneys general for the states of Arizona, Connecticut, Florida, Idaho, Illinois, Kansas, Minnesota, Missouri, Nevada, New York, Ohio, Oregon, Pennsylvania, and Wisconsin. QCC has also settled "do not call" violation investigations by the New York State Consumer Protection Board and the Florida Department of Agriculture and Services. Additionally, in October 2002, the California Public Utilities Commission fined QCC for alleged incidents of slamming and cramming. QCC filed an appeal in California state court, but the appeal was unsuccessful. Copies of the orders or agreements resolving these matters are included in QCC's CC&N Application as Attachment D and Attachment E.

QCC is also involved in two other proceedings in Oklahoma and Delaware. The Oklahoma proceeding is a formal complaint by the Commission Staff involving allegations of one incident of slamming against QCC. QCC states it is in the process of negotiating a settlement of this complaint with the Oklahoma Staff. The Delaware proceeding addressed allegations involving the improper termination of service for 16 customers. QCC states it is in the process of finalizing a settlement agreement with the Delaware Commission to resolve this matter. Final orders on these two proceedings have not yet been issued.

QCC represents that it is also currently cooperating with the attorney general for the State of Missouri regarding certain sales practices, which investigation is ongoing, and is involved in a civil investigation relating to property tax surcharges in North Carolina. QCC is also involved in two pending formal complaints at the FCC; one filed by Touch America, Inc. alleging that QCC and its affiliates violated terms of the U S West, Inc./Qwest Communications Inc. divestiture order and illegally were providing interLATA services in the former U S West local exchange region.

On or about October 25, 2001, a judgment was entered against QCC in Travis County, Texas (matter number 97-13778) in the amount of \$1,746,446. In the lawsuit giving rise to the judgment, AT&T alleged that during construction of QCC's fiber optic network in the vicinity of Austin, Texas, QCC was responsible and liable for three cuts of AT&T fiber. Subcontractors were held to be liable for approximately \$532,000 of the actual damages, and have paid these amounts. The punitive damages portion of the judgment, \$467,808.91, is currently being appealed to the Texas Supreme Court.

Aside from these matters, QCC indicates that, based on its records, it has not been the subject of any other formal complaints or investigation by state or federal utility commissions,

attorneys general, or consumer advocate offices, and similar agencies or entities, regarding its provisions of telecommunications services during the last five years.

As to officers, directors, and managers of QCC: Mark Evans, Vice President and Assistant Treasurer, was named individually in a lawsuit (Civil Case No. 02-RB-464 (PAC)), In re Qwest Savings and Retirement Plan ERISA Litigation, In the United States District Court for the District of Colorado), pursuant to which the plaintiffs (participants of the Qwest Retirement Plan (the "Plan")), allege that the members of the Plan's investment committee (the "Investment Committee") (including Mr. Evans, who was on the Investment Committee) of U S West/Qwest breached their fiduciaries duties by failing "to provide sufficient independent information to participants of the Plan to allow such participants to achieve the stated purpose of the Plan to provide such employees with a voice in the major decisions affecting U S West/Qwest" and "[f]ailing to disclose to participants material information concerning Qwest Fund Shares which they knew of should have known."

5. COMPETITIVE SERVICES ANALYSIS

The Applicant has petitioned the Commission for a determination that the services it is seeking to provide should be classified as competitive. This section of the report addresses Staff's findings regarding the Applicant's request that its services be classified as competitive.

5.1 NOTICE REQUIREMENTS

At this time, the Applicant has not yet published legal notice of the Application in all counties in which it requests authorization to provide service. The Applicant stated in its Application that the legal notice publication will be completed subsequent to the filing date of the Application and upon assignment of a docket number for inclusion in legal notice. QCC will supplement this response once it has received the affidavit of publication.

5.2 COMPETITIVE SERVICES ANALYSIS FOR LOCAL EXCHANGE SERVICES

5.2.1 **A description of the general economic conditions that exist, which makes the relevant market for the service one that, is competitive.**

Some of the local exchange market that the Applicant seeks to enter may have one or more new CLECs that already have been authorized to provide local exchange service. Nevertheless, in locations outside of its service territory which consists of largely rural areas, ILECs hold a virtual monopoly in the local exchange service market. At locations where ILECs provide local exchange service, excluding locations where Qwest is the ILEC that provides local exchange service, the Applicant will be entering the market as an alternative provider of local exchange service and, as such, the Applicant will have to compete with the incumbent provider in order to obtain customers.

5.2.2 The number of alternative providers of the service.

Qwest and various independent LECs are the primary providers of local exchange service in the State. In some of the rural areas that the Applicant seeks to serve and excluding QC's service territory, several CLECs and local exchange resellers are also providing local exchange service.

5.2.3 The estimated market share held by each alternative provider of the service.

Since Qwest and the independent LECs are the primary providers of local exchange service in the State, they have a large share of the market. Since the CLECs and local exchange resellers have only recently been authorized to offer service, they have limited market share.

5.2.4 The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicant, as defined in A.A.C. R14-2-801.

The following are QCC's Arizona Affiliates:

Qwest Corporation (Provides local and intraLATA services.)
1801 California Street, Suite 5100
Denver, CO 80202

Qwest LD Corp. (Provides resold interchange services.)
1801 California Street, Suite 5100
Denver, CO 80202

Qwest Wireless, LLC (Provides CMRS services.)
1801 California Street, Suite 5100
Denver, CO 80202

U S Long Distance, Inc. (Certified provider of alternative operator services.)
1801 California Street, Suite 5100
Denver, CO 80202

5.2.5 The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms and conditions.

ILECs have the ability to offer the same services that the Applicant has requested in their respective service territories. Similarly many of the CLECs and local exchange resellers also offer substantially similar services.

5.2.6 Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).

The local exchange service markets outside of QC's service territory are:

- a. Ones in which ILECs own networks that reach nearly every residence and business in their service territories and which provide them with a virtual monopoly over local exchange service. New entrants are also beginning to enter this market.
- b. Ones in which new entrants will be dependent upon ILECs:
 1. To terminate traffic to customers.
 2. To provide essential local exchange service elements until the entrant's own network has been built.
 3. For interconnection.
- c. Ones in which ILECs have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market and one in which new entrants do not have a long history with any customers.
- d. Ones in which most customers have few choices since there is generally only one provider of local exchange service in each service territory.
- e. Ones in which the Applicant will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

5.3 COMPETITIVE SERVICES ANALYSIS FOR INTEREXCHANGE SERVICES

5.3.1 A description of the general economic conditions that exist, which makes the relevant market for the service one that, is competitive.

The interexchange market that the Applicant seeks to enter is one in which numerous facilities-based and resold interexchange carriers have been authorized to provide service throughout the State. The Applicant will be a new entrant in this market and, as such, will have to compete with those companies in order to obtain customers.

5.3.2 The number of alternative providers of the service.

There are a large number of facilities-based and resold interexchange carriers providing both interLATA and intraLATA interexchange service throughout the State. In addition, various ILECs provide intraLATA interexchange service in many areas of the State.

5.3.3 The estimated market share held by each alternative provider of the service.

The large facilities-based interexchange carriers (AT&T, Sprint, MCI WorldCom, etc.) hold a majority of the interLATA interexchange market, and the ILECs provide a large portion of the intraLATA interexchange market. Numerous other interexchange carriers have a smaller part of the market and one in which new entrants do not have a long history with any customers.

5.3.4 The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicant, as defined in A.A.C. R14-2-801.

The following are QCC's Arizona Affiliates:

Qwest Corporation (Provides local and intraLATA services.)
1801 California Street, Suite 5100
Denver, CO 80202

Qwest LD Corp. (Provides resold interchange services.)
1801 California Street, Suite 5100
Denver, CO 80202

Qwest Wireless, LLC (Provides CMRS services.)
1801 California Street, Suite 5100
Denver, CO 80202

U S Long Distance, Inc. (Certified provider of alternative operator services.)
1801 California Street, Suite 5100
Denver, CO 80202

5.3.5 The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms and conditions.

Both facilities-based and resold interexchange carriers have the ability to offer the same services that the Applicant has requested in their respective service territories. Similarly many of the ILECs offer similar intraLATA toll services.

5.3.6 Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).

The interexchange service market is:

- a. One with numerous competitors and limited barriers to entry.
- b. One in which established interexchange carriers have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market.

- c. One in which the Applicant will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

6. RECOMMEDATIONS

This section of the report addresses Staff's overall recommendations with respect to any conditions that it believes should be made a part of any CC&N that is granted by the Commission.

6.1 RECOMMENDATIONS ON THE APPLICATION FOR A CC&N

Staff recommends that the application for a CC&N to provide intrastate telecommunications services, as listed in Section 2.2 of this report, be granted. In addition, Staff further recommends:

1. That, unless it provides services solely through the use of its own facilities, the Applicant procure an Interconnection Agreement before being allowed to offer local exchange service. The interconnection agreement should be procured within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission. If the Applicant provides services solely through the use of its own facilities, no other information shall be required once the Applicant informs the Commission of that fact by a letter with the Commission's Docket Control Center under the same timeframe and provision of service criteria as above¹²;
2. That the Applicant files with the Commission's Docket Control Center its plan to have its customers' telephone numbers included in the incumbent's Directories and Directory Assistance Databases. This information should be filed within 365 days of the effective date of the order in this matter or 30 days prior to the provision of service, whichever comes first, and must remain in effect until further order of the Commission;
3. That the Applicant pursue permanent number portability arrangements with other LECs pursuant to Commission rules, federal laws and federal rules;
4. That the Applicant agree to abide by and participate in the AUSF mechanism instituted in Decision No. 59623, dated April 24, 1996 (Docket No. RT-00000E-95-0498);
5. That the Applicant abides by the quality of service standards that were approved by the Commission for Qwest in Docket No. T-01051B-93-0183;

¹² This should in no way be constructed as a finding by the Commission under Section 251 (f) of the Telecommunications Act of 1996.

6. That the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve areas where the Applicant is the only provider of local exchange service facilities;
7. That the Applicant be required to abide by all the Commission decisions and policies regarding CLASS services;
8. That the Applicant be required to provide 2-PIC equal access;
9. That the Applicant be required to notify the Commission immediately upon changes to the Applicant's name, address or telephone number;
10. That the Applicant comply with all Commission rules, orders, and other requirements relevant to the provision of intrastate telecommunications service;
11. That the Applicant maintain its accounts and records as required by the Commission;
12. That the Applicant file with the Commission all financial and other reports that the Commission may require, and in a form and at such times as the Commission may designate;
13. That the Applicant maintain on file with the Commission all current tariffs and rates, and any service standards that the Commission may require;
14. That the Applicant cooperate with Commission investigations including, but not limited to, customer complaints;
15. That the Applicant participate in and contribute to a universal service fund, as required by the Commission;
16. That the Applicant be subject to the Commission's rules and the 1996 Telecommunications Act to the extent that they apply to CLECs;
17. The maximum rates for these services should be the maximum rates proposed by the Applicant in its proposed tariffs. The minimum rates for the Applicant's competitive services should be the Applicant's total service long run incremental costs of providing those services as set forth in AAC R14-2-1109;
18. That the Commission authorize the Applicant to discount its rates and service charges to the marginal cost of providing the services;
19. That QCC should initially be approved to provide service only in areas outside of QC's service territory;
20. Staff obtained information from QCC regarding its fair value rate base. As reported in the Applicant's Application, QCC's fair value rate base is captured in the consolidated

financial statement, together with QCII's other subsidiaries. However, the rate to be ultimately charged by QCC for the local exchange service(s) will be influenced by the market. QCC would initially be providing service in areas where various local exchange carriers are providing telephone service. Therefore, the Applicant would have to compete with those providers in order to obtain subscribers to its service. The Applicant will face competition from other competitive providers in offering service to its potential customers. Therefore, the competitive process should result in rates that are just and reasonable. Because of the nature of the competitive market and other factors, a fair value analysis is not necessarily representative of the Company's operations;

21. The Applicant should be ordered to file an application with the Commission pursuant to AAC R14-2-1107, if the Applicant desires to discontinue service. The Applicant should be required to notify each of its customers and the Commission 60 days prior to filing an application to discontinue service; and any failure to do so should result in forfeiture of the Applicant's performance bond; and
22. The Applicant should be required to notify the Commission before providing service to any unserved areas in the state.

Staff further recommends that the Applicant be ordered to comply with the following. If it does not do so, the Applicant's CC&N shall be null and void without further order of the Commission and no time extensions shall be granted.

1. The Applicant shall file conforming tariffs for its CC&Ns to provide resold long distance, facilities-based long distance, resold local and facilities-based local exchange service within 365 days from the date of an Order in this matter or 30 days prior to providing service, whichever comes first, and in accordance with the Decision;
2. QCC's tariff, however, does need to be modified to reflect the limitation Staff proposes on the service area for QCC's provision of resold and facilities-based local exchange service. In addition, QCC needs to modify its Arizona Tariff No. 3 Section 2.2.5 item E to ensure that local exchange telecommunications services will not be provided to business customers participating in the Competitive Response Program.
3. In the Applicant's tariffs, both an initial rate (the actual rate to be charged) and a maximum rate must be listed for each competitive service offered, provided that the rate for the service is not less than the Company's total service long-run incremental cost of providing the service pursuant to A.A.C. R14-2-1109.
4. The Applicant shall:
 - a. Procure an additional performance bond equal to \$135,000. The minimum bond amount of \$135,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The bond amount should be increased in increments of \$67,500. This

increase should occur when the total amount of the advances, deposits, and prepayments is within \$13,500 of the bond amount.

- b. Docket proof of the performance bond within 365 days of the effective date of an Order in this matter or 30 days prior to the provision of service, whichever comes first. The performance bond must remain in effect until further order of the Commission.
- c. If at some time in the future, the Applicant does not collect from its customer advances, deposits, and/or prepayments, Staff recommends that the Applicant be allowed to file a request for cancellation of its established performance bond regarding its resold long distance services. Such request must reference the decision in this docket and must explain the applicant's plans for canceling those portions of the bond.

6.2 RECOMMENDATION ON THE APPLICANT'S PETITION TO HAVE ITS PROPOSED SERVICES CLASSIFIED AS COMPETITIVE

Staff believes that the Applicant's proposed services should be classified as competitive. There are alternatives to the Applicant's services. The Applicant will have to convince customers to purchase its services, and the Applicant has no ability to adversely affect the local exchange or interexchange service markets outside of its affiliate QC's service territory. Therefore, the Applicant will have no market power in the local exchange or interexchange service markets where alternative providers of telecommunications services exist. Staff therefore recommends that the Applicant's proposed services be classified as competitive.

EXHIBIT A
QCC'S CERTIFICATES: TYPE OF TELECOMMUNICATION SERVICES BY STATES

Type of Telecommunications Services *

No.	States	Facilities-Based LD Services	Resold LD Services	Facilities-Based CLEC Services	Resold CLEC Services
1	Alabama	X	X		
2	Arkansas		X		
3	California	X	X		
4	Colorado			X	
5	Connecticut		X	X	X
6	Delaware		X	X	X
7	District of Columbia			X	X
8	Florida	X	X	X	X
9	Georgia	X	X	X	X
10	Hawaii		X		
11	Idaho			X	
12	Illinois	X	X	X	X
13	Indiana	X	X	X	
14	Iowa			X	
15	Kansas	X	X	X	
16	Kentucky	X	X	X	
17	Louisiana	X	X		
18	Maine	X	X		
19	Maryland	X	X	X	
20	Massachusetts	X	X	X	X
21	Michigan	X	X	X	X
22	Minnesota			X	
23	Mississippi	X	X	X	X
24	Missouri	X	X	X	X
25	Montana			X	
26	Nevada	X	X	X	X
27	New Hampshire	X	X	X	
28	New Jersey	X	X	X	X
29	New York	X	X	X	X
30	North Carolina	X	X	X	X
31	Ohio	X	X	X	
32	Oklahoma	X	X	X	
33	Oregon			X	
34	Pennsylvania	X	X	X	
35	Rhode Island		X	X	
36	South Carolina	X	X	X	
37	Tennessee		X	X	
38	Texas	X	X	X	
39	Utah			X	
40	Vermont		X	X	
41	Virginia	X	X	X	X
42	Washington			X	
43	West Virginia	X	X	X	
44	Wisconsin		X	X	
45	Wyoming			X	

(X) Indicates the type of telecommunications services that QCC is certified to provide in each of the states listed.

(*) QCC's response to Section (A-19) in their Application.

EXHIBIT B
FINANCIAL RATIOS

Qwest Communications Corporation
Docket No. T-02811B-04-0313

	Qwest* Financial Ratios	Telecom Industry Average	
LIQUIDITY RATIOS:			
Current Ratio: Current assets/ Current Liabilities	0.8	0.9	(a)
Qwest current ratio is less than the industry average.			
ASSET MANAGEMENT RATIOS			
Total Assets Turnover Ratio: Sales/ Total Assets	0.5	0.4	(a)
Ratio measures the utilization of Qwest's total assets, which is above the industry average.			
DEBT MANAGEMENT RATIOS			
Total Debt to Total Assets: Total debt/ Total assets	0.7	NA	(a)
Ratio measures the percentage of total funds provided by creditors			
CAPITALIZATION STRUCTURE:			
Common Equity Ratio	-6%	55%	(b)
Long-Term Debt Ratio	106%	45%	(b)

Compared to the telecom industry average, Qwest's capitalization structure shows that it has negative equity and relies entirely on long-term debt.

(*)Data represents Qwest Communications International Inc.
NA = Not Available

Sources: Industry Average

(a) [Interhttp://partners.thomsoninvest.net/brokerage/cgi-bin/info](http://partners.thomsoninvest.net/brokerage/cgi-bin/info)

(b) TheValue Line Investment Survey, Issue 5, October 1, 2004, Page 719.

EXHIBIT C
LOCAL EXCHANGE CALLING PLANS AND CHARGES

Qwest Communications Corporation
Docket T-02811B-04-0313

Rates and Charges
By Competing Local Exchange Carriers

LOCAL EXCHANGE CALLING PLANS	QCC	Cox	AT&T	Sprint	Qwest
BUSINESS PLANS:					
Basic Main Line Service	\$45.00	\$30.00	\$29.50	\$59.95	\$30.40
Additional Line Service	\$45.00	\$30.00	\$29.50	\$59.95	\$30.40

Notes:

QCC

* Tariff does not include a specific additional line monthly rate; assumed to equal main line rate

Cox

* Arizona C.C. Tariff No. Sixth Revised
Page No. 61

AT&T

* Local Exchange Services Tariff, Price List, Original Page 1

Sprint

* Arizona C.C. Local Exchange, tariff No. 4, Original Page 63.5

Qwest

*Exchange & Network Services Price Cap
Tariff, Section 5, Page 22, Release 4